

# The Federal Tax Treatment of Married Same-Sex Couples

Updated July 30, 2015

Congressional Research Service

<https://crsreports.congress.gov>

R43157

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## Scope of the Report

This report provides an overview of the federal tax treatment of same-sex married couples, with a focus on the federal income tax. Estate tax issues are also discussed.<sup>1</sup> The administration of federal tax laws for married same-sex couples changed as a result of the U.S. Supreme Court ruling in *United States v. Windsor*<sup>2</sup> in 2013, striking down Section 3 of the Defense of Marriage Act. The administration of federal tax laws was not affected by the June 26, 2015, ruling in *Obergefell v. Hodges*.<sup>3</sup> *Obergefell* struck down state bans on same-sex marriage, holding that all states must both permit same-sex couples to marry in their states and recognize same-sex marriages that were formed in other states. While it did not change the administration of federal income tax laws, the *Obergefell* decision may affect the number of same-sex couples who decide to marry (and hence the number of federal and state tax returns filed by married couples). Analysis of changes to individuals' state tax liabilities resulting from the *Obergefell* decision is beyond the scope of this report; however, state tax changes may ultimately affect federal tax liabilities for those couples who itemize deductions on their federal returns.<sup>4</sup>

This report focuses on changes in the *interpretation and administration* of federal tax law resulting from the Court's *Windsor* decision. The decision itself did not amend federal tax law. This report is not intended to address *all* tax-related issues that may arise as a result of the federal recognition of same-sex marriages for tax purposes. Such discussion is beyond the scope of this report.

## United States v. Windsor

On June 26, 2013, the U.S. Supreme Court held that Section 3<sup>5</sup> of the Defense of Marriage Act (DOMA)<sup>6</sup> was unconstitutional. Section 3 required that, for purposes of federal enactments, marriage be defined as the union of one man and one woman and the word spouse be defined as someone of the opposite-sex who is a husband or wife.<sup>7</sup> Hence, before the *Windsor* decision,

<sup>1</sup> Although the estate tax was the motivating issue in the *Windsor* decision, as discussed later in this report, few married same-sex couples will likely be affected by changes in the administration of the estate tax.

<sup>2</sup> *United States v. Windsor*, 570 U.S. \_\_\_\_; 133 S. Ct. 2675 (2013). No. 12-307, slip op. available at [http://www.supremecourt.gov/opinions/12pdf/12-307\\_6j37.pdf](http://www.supremecourt.gov/opinions/12pdf/12-307_6j37.pdf).

<sup>3</sup> *Obergefell v. Hodges*, 576 U. S. \_\_\_\_ (June 26, 2015), No. 14-556, slip op. available at [http://www.supremecourt.gov/opinions/14pdf/14-556\\_3204.pdf](http://www.supremecourt.gov/opinions/14pdf/14-556_3204.pdf).

<sup>4</sup> State income taxes that are withheld, paid in as estimated taxes, paid with an extension request, or paid to satisfy a balance due on a completed tax return or assessment from the state for income taxes may be itemized on Schedule A, which is attached to Form 1040. For any year in which a taxpayer has an overpayment of state taxes, that overpayment generally will be included in the taxpayer's federal income for the year in which a refund is received or the overpayment amount is credited to the taxpayer's account. Thus, for those who itemize deductions, the state tax liability may result in either a reduction in the federal income tax liability or an increase.

<sup>5</sup> 1 U.S.C. § 7.

<sup>6</sup> P.L. 104-199.

<sup>7</sup> According to Section 3 of the Defense of Marriage Act (DOMA), "In determining the meaning of any Act of Congress, or of any ruling, regulation, or interpretation of the various administrative bureaus and agencies of the United States, the word 'marriage' means only a legal union between one man and one woman as husband and wife, and the word 'spouse' refers only to a person of the opposite-sex who is a husband or a wife." 1 U.S.C. § 7. The *Windsor* decision arose in the context of a dispute over estate tax liability. When Edith Windsor's wife died, her wife's estate was obligated to pay approximately \$363,000 in federal estate taxes. Had Edith Windsor been married to a man, she would have qualified for the spousal exemption and the estate would not have been taxed at the time of her spouse's death.

same-sex marriages *were not recognized* by the federal government for the receipt of federal benefits or for federal tax purposes. The Government Accountability Office (GAO) estimated that in 2004 (the most recent estimates available) there were 1,138 statutory provisions in the U.S. Code in which marital status was a factor in determining benefits.<sup>8</sup> Of these, almost 200 were statutory provisions of the Internal Revenue Code (IRC).<sup>9</sup>

## Same-Sex Marriage Recognition and the Internal Revenue Code (IRC)

As a result of the *Windsor* decision, on August 29, 2013, the Department of the Treasury and Internal Revenue Service (IRS) ruled that all legal same-sex marriages would be recognized for federal tax purposes, and that, “[f]or federal tax purposes, the terms ‘spouse,’ ‘husband and wife,’ ‘husband,’ and ‘wife’ include an individual married to a person of the same sex if the individuals are lawfully married under state law, and the term ‘marriage’ includes such a marriage between individuals of the same sex.”<sup>10</sup> At the time, IRS Revenue Ruling 2013-17 (the 2013 IRS ruling) applied regardless of whether the couple resided in a state or jurisdiction that recognized same-sex marriage.<sup>11</sup> Thus, for federal tax purposes, same-sex couples who were legally married in one state, but resided in a state that did not recognize the marriage at that time, would be treated as married.<sup>12</sup> As a result of *Obergefell*, states and other jurisdictions must now allow and recognize same-sex marriages, making this distinction moot.

The 2013 IRS ruling did not apply to civil unions, registered domestic partnerships, or other formal relationships not denominated as a marriage under state law.<sup>13</sup> *Obergefell* does not change this.

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<sup>8</sup> U.S. General Accounting Office, *Defense of Marriage Act: Update to Prior Report*, GAO-04-353R, January 23, 2004.

<sup>9</sup> Using tables provided by GAO, CRS found that in 2004, there were 198 sections of the Internal Revenue Code (IRC) in which marital status was a factor. See Appendix 1 and Appendix 2 in GAO-04-353R and Enclosure II in U.S. General Accounting Office, *Defense of Marriage Act*, OGC-97-16, January 31, 1997.

<sup>10</sup> Rev.Rul.2013-17, 2013-38 I.R.B. Available at [http://www.irs.gov/irb/2013-38\\_IRB/ar07.html](http://www.irs.gov/irb/2013-38_IRB/ar07.html). Although it may be necessary to modify wording in other titles of the U.S. Code or respective regulations to assure application to married same-sex couples, the 2013 IRS ruling makes it unnecessary to revise the wording in the Internal Revenue Code (IRC). Nonetheless, legislation introduced in the 114<sup>th</sup> Congress (e.g., S. 1740) may clarify that all provisions of the IRC apply equally to both opposite-sex and same-sex married couples.

<sup>11</sup> Similarly, guidance from the Office of Personnel Management indicated that, for purposes of eligibility for specific federal employee benefits, legal same-sex marriages would be recognized “regardless of an employee’s or annuitant’s state of residency.” OPM, Benefits Administration Letter, No. 13-203 (Jul. 17, 2013). Available at <http://www.opm.gov/retirement-services/publications-forms/benefits-administration-letters/2013/13-203.pdf>.

<sup>12</sup> This ruling clarified previous uncertainty over whether recognition of same-sex marriage for federal tax purposes would depend on recognition of same-sex marriage in a couple’s state of residence. The Court in the *Windsor* decision wrote, “The federal statute is invalid, for no legitimate purpose overcomes the purpose and effect to disparage and to injure those whom the State, by its marriage laws, sought to protect in personhood and dignity. By seeking to displace this protection and treating those people as living in marriages less respected than others, the federal law is in violation of the Fifth Amendment. This opinion and its holding are confined to those lawful marriages.” *U.S. v. Windsor*, 570 U.S. \_\_\_\_; 133 S.Ct. at 2696. No. 12-307, slip op. at 25-26 available at [http://www.supremecourt.gov/opinions/12pdf/12-307\\_6j37.pdf](http://www.supremecourt.gov/opinions/12pdf/12-307_6j37.pdf).

<sup>13</sup> It is important to note that a civil union is a legal protection conferred at the state, not the federal, level. As such, a variety of benefits discussed in this report may not apply to civil unions.

## Tax Issues

With respect to federal tax-related issues, the 2013 IRS ruling primarily affected married same-sex couples' federal income taxes. For the limited number of married same-sex individuals who had sufficient assets to be subject to the estate tax, potential estate tax liability may also have been affected.

Treating same-sex couples as married for federal tax purposes could have substantial financial implications for some affected couples. The budgetary impact from the perspective of the federal government, however, is likely small.<sup>15</sup> The U.S. Census Bureau estimates that in 2013 there were 726,600 same-sex couple households in the United States (approximately one-half of one percent of all tax returns filed), of which approximately 251,695 (34.6%) self-identify as married.<sup>16</sup>

### Estate Tax

Under current law, a deceased spouse's estate can transfer all of its assets to the surviving spouse without incurring any estate tax.<sup>17</sup> Before the decision in *Windsor*, a married same-sex couple was not eligible for this spousal tax exemption because, due to Section 3 of DOMA, same-sex marriages *were not recognized* by the federal government for the receipt of federal benefits or for federal tax purposes. (The exemption amount is the amount of the estate which, when bequeathed to an heir, is tax-free. If the heir is a spouse, the exemption amount is unlimited.) Thus, for some couples, federal recognition of same-sex marriage for tax purposes could result in a reduced estate tax liability.<sup>18</sup>

#### IRS's Revenue Ruling 2013-17

The IRS's Revenue Ruling 2013-17<sup>14</sup> "provides guidance on the effect of the *Windsor* decision on the [Internal Revenue] Service's interpretation of the sections of the Code that refer to taxpayers' marital status."

According to the IRS, at the time of the *Windsor* decision "there [were] more than two hundred Code provisions and Treasury regulations relating to the internal revenue laws that include the terms 'spouse,' 'marriage' (and derivatives thereof, such as 'marries' and 'married'), 'husband and wife,' 'husband,' and 'wife.'"

The revenue ruling concluded "that gender-neutral terms in the [Internal Revenue] Code that refer to marital status, such as 'spouse' and 'marriage,' include, respectively, (1) an individual married to a person of the same-sex if the couple is lawfully married under state law, and (2) such a marriage between individuals of the same-sex." In addition, the ruling concluded that "the terms 'husband and wife,' 'husband,' and 'wife' should be interpreted to include same-sex spouses."

Revenue Ruling 2013-17 hence requires married same-sex couples to be treated as married for federal tax purposes, without the need for legislation to redefine the terms "marriage," "spouse," "husband", or "wife." The same may not be true of other federal benefits or programs, where redefining these terms in light of *Windsor* may affect the administration of non-tax laws.

<sup>14</sup> Rev.Rul.2013-17, 2013-38 I.R.B. Available at [http://www.irs.gov/irb/2013-38\\_IRB/ar07.html](http://www.irs.gov/irb/2013-38_IRB/ar07.html)

<sup>15</sup> Lydia Beyoud, "Domestic Partners: Practitioners Say Major Guidance Needed from Federal Agencies for Same-Sex Couples," *BNA Daily Tax Report*, July 1, 2013. The effect of federal recognition of same-sex marriages on federal tax revenue is also discussed below in "Potential Federal Tax Revenue Consequences of Federal Recognition of Same-Sex Marriage."

<sup>16</sup> These data are reported as the percentage of same-sex households where the partners are reported as spouses on the American Community Survey (ACS). It does not necessarily reflect those spouses who are legally married. Partners in same-sex couples may consider themselves "spouses" even if they are not legally married if, for example, they are in a civil union or a domestic partnership. Hence these statistics should not be interpreted as the number of same-sex couples who are legally married. For ACS data see <http://www.census.gov/hhes/samesex/data/acs.html>.

<sup>17</sup> For an overview of the estate tax, see CRS Report R42959, *Recent Changes in the Estate and Gift Tax Provisions*, by Jane G. Gravelle; and CRS Report R43576, *Estate and Gift Taxes for Nonresident Aliens*, by Emily M. Lanza.

<sup>18</sup> Recognition of same-sex marriages for the purposes of the federal estate tax can only result in a reduction in estate

In addition to being eligible for unlimited spousal transfers, same-sex couples may also benefit from transferability of exemption amounts to non-spouse beneficiaries. Unlike the unlimited spousal exemption, there is a limit on the amount of an estate which can pass to a non-spouse heir tax-free. As enacted, the estate tax is structured so that the first \$5 million per individual or \$10 million per federally recognized married couple (adjusted for inflation) of the estate and inter vivos gifts (gifts made prior to death) are exempt from federal taxes when bequeathed to non-spouse beneficiaries, like children or non-relatives.<sup>19</sup>

In 2015, once adjusted for inflation, the exemption amount per individual is \$5.43 million. Since any unused exemption amounts are transferable between spouses, if one spouse leaves an estate of \$3 million upon death in 2015 to a non-spouse beneficiary, the remaining \$2.43 million of that deceased spouse's exemption amount would be transferred to the surviving spouse.<sup>20</sup> Hence, the surviving spouse's exemption amount would increase from \$5.43 million (or, the amount of the exemption in the year the second spouse dies) to \$7.86 million. Before the *Windsor* decision, the surviving same-sex spouse could only use his or her own exemption amount to make a tax-free bequest to a non-spouse beneficiary (\$5.43 million in 2015). Hence, the surviving spouse of a same-sex marriage may now be able to bequeath a greater amount tax-free to a non-spouse beneficiary.

Although federal recognition of same-sex marriages may benefit affluent married same-sex couples, it may have no effect on the majority of those couples because most people's estates generally are not subject to the estate tax. In 2013, roughly 3,800 estates, representing less than 0.2% of all deaths in 2013, were subject to the estate tax.<sup>21</sup> Given that so few estates are subject to the estate tax, and that the estate tax is a small portion of overall federal tax revenues,<sup>22</sup> the federal budgetary impact of recognizing same-sex marriages for estate tax purposes is small.<sup>23</sup>

## Income Tax

Federal recognition of same-sex marriages affects married same-sex couples' federal income taxes in a variety of ways. All taxpayers in legally established same-sex marriages are required to file as married on any return filed after September 15, 2013,<sup>24</sup> which may affect their marginal tax rates.<sup>25</sup> Other tax effects may include changes in eligibility for a variety of tax credits, as well as changes in the tax treatment of certain forms of employee compensation. These changes will, in many cases, change married same-sex couples' tax liabilities, as discussed below. There are other changes not discussed which are beyond the scope of this report.

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taxes. This yields a so-called "marriage tax bonus" for the taxpayer.

<sup>19</sup> This exemption amount is adjusted annually for inflation.

<sup>20</sup> An estate tax return must be timely filed to affect this transfer *even if* the estate would not otherwise be required to file a return.

<sup>21</sup> See Tax Policy Center's Tax Topic's overview of current estate tax issues, available at <http://www.taxpolicycenter.org/taxtopics/estatetax.cfm>.

<sup>22</sup> In 2012, 1.2% of total federal revenue was collected through the estate tax.

<sup>23</sup> This was the conclusion reached in a 2004 Congressional Budget Office (CBO) report. CBO also noted that same-sex spouses may be more likely than opposite-sex spouses to make charitable bequests from their estates, although no specific evidence was given in support of this claim. See Congressional Budget Office, *The Potential Budgetary Impact of Recognizing Same-Sex Marriages*, Washington, DC, June 21, 2004, <http://www.cbo.gov/publication/15740>.

<sup>24</sup> September 16, 2013, is the effective date of IRS Revenue Ruling 2013-17.

<sup>25</sup> 26 U.S.C. §§1(a), (d); 6013; 7703.

## Tax Filing Status and Tax Brackets

Before *Windsor*, married same-sex couples were generally considered unmarried for federal income tax purposes, and each person would generally file as single if the couple was childless. In cases where the couple had children, one partner would claim any children as dependents and file federal income taxes using the head of household status. The other spouse would file as single.

Legally married same-sex couples are now required to file their taxes in the same manner as legally married opposite-sex couples—generally either jointly (“married filing jointly”) or separately (“married filing separately”). However, few married taxpayers file separately (less than 5% of married taxpayers in 2012)<sup>26</sup> because it typically results in higher tax liabilities than if income taxes are filed jointly.<sup>27</sup> Hence, the remainder of this report will generally describe situations where married same-sex couples file their returns jointly.

For some same-sex couples filing their returns jointly could result in increased or decreased income tax liabilities. Some married same-sex couples may face a “marriage penalty,” having a higher tax liability when filing taxes as a married couple than their combined tax liability when filing as two unmarried taxpayers. Other married same-sex couples may benefit from a “marriage bonus,” whereby they have a lower tax liability when filing as a couple than their combined tax liability when filing as unmarried individuals.

Various circumstances may make it more or less likely that couples incur a marriage penalty or a marriage bonus when filing their income taxes.<sup>28</sup> Marriage penalties are more likely among couples where both partners earn similar incomes. Couples with a greater disparity in earnings are more likely to experience a marriage bonus. Most couples in which one spouse earns less than 5% (or none) of the family’s total income will experience a marriage bonus.<sup>29</sup>

Marriage tax penalties and bonuses are consequences of a progressive tax system, whereby higher ranges of income are subject to higher tax rates. Tax brackets refer to the range of income subject to a particular tax rate. For example, under current law, the first \$18,450 of taxable income for all married joint filers is subject to a 10% tax rate (the “10% bracket”). Taxable income above \$18,450 but less than \$74,900 is taxed at a 15% rate (the “15% bracket”). All tax brackets for 2015 for single and married joint filers are given in the text box on the following page.

**Table 1** provides an illustrative example of how the distribution of a combined income of \$200,000 between partners can result in a marriage bonus or penalty. A couple where both partners earn \$100,000, having a combined income of \$200,000, would experience a marriage tax

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<sup>26</sup> In 2012, 56.4 million married taxpayers filed income tax returns, of which 2.7 million were filed as married filing separately. See the IRS Statistics of Information (SOI), Table 1.2, <http://www.irs.gov/uac/SOI-Tax-Stats—Individual-Statistical-Tables-by-Size-of-Adjusted-Gross-Income>.

<sup>27</sup> Filing separately tends to be least advantageous to married couples, since they are denied a variety of tax benefits or receive smaller benefits. See Leslie A. Whittington and Updated by James Alm, “Marriage Penalty,” in *The Encyclopedia of Taxation and Tax Policy*, ed. Joseph J. Cordes, Robert D. Ebel and Jane G. Gravelle, 2<sup>nd</sup> ed. (Washington, D.C.: The Urban Institute Press, 2005), p. 252.

<sup>28</sup> For evidence on the tax consequences of marriage for cohabiting couples, see Emily Y. Lin and Patricia K. Tong, “Marriage and Taxes: What Can We Learn from Tax Returns Filed by Cohabiting Couples?” *National Tax Journal*, vol. 65, no. 4 (December 2012), pp. 807-826.

<sup>29</sup> *Ibid.*, p. 818. Using 2007 data, it was found that only 3% of cohabiting couples where one spouse earned less than 5% of combined income prior to marriage experienced a marriage tax penalty, 21% saw no change in tax liability, and 77% had a marriage bonus.



penalty of \$855. A couple where one partner earns \$50,000 and the other \$150,000, also having a combined income of \$200,000, would have a marriage tax bonus of \$620.

In the example in **Table 1**, when each taxpayer earning \$100,000 was taxed as a single individual, each had earnings that put them in the lower end of the 28% tax bracket. Thus, most of their income fell into the 25% bracket or below. A feature of the U.S. income tax system is that the 25% tax bracket for married filing jointly is *less than twice* as large as the 25% bracket for singles.<sup>30</sup> Hence, when treated as a married couple, a greater proportion of the couples' combined income falls into the higher 28% tax bracket. The marriage tax penalty results from a greater proportion of the couples' combined income being taxed at the 28% rate.

**Table 1. Example of Marriage Penalties and Bonuses Among Same-Sex Couples**

Ordinary Income Split between Partners	Combined Tax Liability		Change in Tax Liability
	Unmarried Partners	Married Partners	
Partner A: \$50,000 Partner B: \$150,000	\$37,935	\$37,315	\$620 (bonus)
Partner A: \$100,000 Partner B: \$100,000	\$36,460	\$37,315	-\$855 (penalty)

**Source:** 2015 Data from the Tax Policy Center. See <http://taxpolicycenter.org/taxfacts/marriagepenaltycalculator.cfm>.

The 2001 and 2003 tax cuts (which were extended permanently for most taxpayers by the American Taxpayer Relief Act of 2012 [P.L. 112-240]) reduced or eliminated marriage penalties for many middle-income taxpayers.<sup>31</sup> One way these laws reduced marriage penalties was by making certain tax brackets for married joint filers twice as large as the equivalent bracket for single filers.<sup>32</sup> Specifically, the 2001 and 2003 tax cuts increased the size of the 10% and 15% tax brackets for married taxpayers filing jointly such that brackets for married filing jointly became twice the size of single brackets (as illustrated in **Table 2**).<sup>33</sup> Hence, if two single individuals in the 10% or 15% bracket marry, their combined income would either still be in the 15% bracket (marriage would be tax-neutral) or in the 10% bracket (a marriage bonus since a portion of their income would be taxed at a lower rate, 10% versus 15%).

<sup>30</sup> The size of a tax bracket can be thought of as the amount of taxable income subject to a particular tax rate. In the case of the 25% bracket, \$53,300 of income between \$37,450 and \$90,750 is taxable at the 25% rate for singles. For married couples, \$76,300 of taxable income between \$74,900 and \$151,200 is taxable at the 25% rate. Hence the size of the 25% bracket for married filers (\$76,300) is 167%—less than twice the size—of the bracket for singles (\$53,300).

<sup>31</sup> For more information on all the provisions of the Bush-era tax cuts, including marriage penalty relief, see Table 1 in CRS Report R42894, *An Overview of the Tax Provisions in the American Taxpayer Relief Act of 2012*, by Margot L. Crandall-Hollick.

<sup>32</sup> A tax bracket is a range of income that is subject to a specific tax rate. (For example, if hypothetically income between \$10,000 and \$20,000 was subject to a 7% tax rate, that range of income would be called the 7% tax bracket.)

<sup>33</sup> The 2001 and 2003 tax cuts made the standard deduction for married couples twice as large as the standard deduction for individuals and coordinated phase-out thresholds for certain tax benefits. These provisions were made permanent by P.L. 112-240.



**Table 2. Tax Brackets for Single Filers, Head of Household Filers, and Married Joint Filers, 2015**

Bracket (tax rate)	Single	Head of Household	Married Filing Jointly
	Taxable Income (over-but not over)	Taxable Income (over-but not over)	Taxable Income (over-but not over)
10%	\$0-\$9,225	\$0-\$13,150	\$0-\$18,450
15%	\$9,225-\$37,450	\$13,150-\$50,200	\$18,450-\$74,900
25%	\$37,450-\$90,750	\$50,200-\$129,600	\$74,900-\$151,200
28%	\$90,750-\$189,300	\$129,600-\$209,850	\$151,200-\$230,450
33%	\$189,300-\$411,500	\$209,850-\$411,500	\$230,450-\$411,500
35%	\$411,500-\$413,200	\$411,500-\$439,000	\$411,500-\$464,850
39.6%	\$413,200	\$439,000-	\$464,850-

**Source:** IRS Revenue Procedure 2014-61

As an example, take a single taxpayer with taxable income of \$1,000. This taxpayer would be in the 10% bracket. Suppose this taxpayer marries an individual with taxable earnings of \$10,000, putting them in the 15% bracket for individuals. With a combined income of \$11,000, this couple would be in the 10% bracket when married filing jointly. With no income being taxed at the 15% rate, this couple would experience a marriage tax bonus. Dual-worker couples with income above the 15% bracket threshold could face a penalty because higher tax brackets for joint filers are less than twice as wide as those for single filers. Ultimately for those taxpayers with income above the 15% bracket (\$37,450 for singles and \$74,900 for joint filers in 2015), the distribution of income between both spouses and the presence or absence of children will determine whether marriage results in a penalty or bonus.

Marriage penalties may be more likely for couples with children for several reasons. Many involve tax credits, which are discussed below. However, another reason involves the changes in filing status and resulting changes in tax brackets. Before the *Windsor* decision, married same-sex couples with children could not file a federal tax return as a married couple. Instead, in many cases one partner would file as a head of household, claiming the children as dependents. The other would file as single. Same-sex couples who are married with children are now required to file as married. Such couples may find that they will be in a higher tax bracket when filing joint returns than they were when they filed as head of household and single. Since tax brackets above the 15% bracket for married couples filing jointly are less than the combined equivalent levels if one of the taxpayers were filing as head of household and the other as single, married same-sex couples may be subject to a marriage penalty depending on the distribution of earnings between the spouses.

### Other Selected Income Tax Issues

Federal recognition of same-sex marriages may affect other aspects of married same-sex couples' income taxes, including the amount of or eligibility for credits and the tax treatment of certain forms of employee compensation.

## Income Tax Credits

Marriage can affect the amount of certain tax credits, especially those that benefit taxpayers with children. Generally, tax credits are structured such that the amount of the credit falls when income exceeds a certain threshold, ultimately phasing out to zero. When marriage results in a combined income that is in a credit's phase-out range (or is so high the taxpayers are ineligible for the credit), the credit amount may be reduced, resulting in increased tax liability. Some of the credits that are subject to income limitations are described below:

- **The Earned Income Tax Credit (EITC):** The value of the earned income tax credit (EITC) is reduced for many low-income dual earner couples when they are married. Marriage penalties occur when the joint income of the married couple pushes them into the EITC phase-out range or results in the couple being ineligible for the credit.<sup>34</sup>
- **The Child and Dependent Care Credit:** The amount of the child and dependent care credit is limited to no more than the income of the lower earning spouse. If one spouse has no income, the couple generally would not qualify for the credit.
- **The Child Tax Credit:** The value of the child tax credit phases out as a taxpayer's income rises above a certain income level.<sup>35</sup> The phase-out threshold for married couples is less than twice that for unmarried individuals. As a result, two unmarried individuals might each qualify for the credit but receive a smaller credit or become ineligible for it if married.
- **Education Tax Credits:** The income levels at which taxpayers are ineligible for education tax credits tend to be twice as high for married couples as for singles. The ultimate value of the credit as a result of marriage will depend on the distribution of income among spouses. Marriage is unlikely to affect the overall credit amount among couples whose income is equally distributed between the two partners. However, among couples whose income is less evenly distributed, the value of their education credit will depend on the income level of the individuals who incur education expenses, and could increase or decrease as a result of marriage depending on the taxpayers' particular circumstances.
- **Adoption Credit:** The *Windsor* decision also had implications for same-sex couples claiming the adoption tax credit. The adoption credit is generally not allowed when adopting a spouse's child.<sup>36</sup> Therefore, as a result of the *Windsor* decision some same-sex partners who might otherwise have been able to claim an adoption credit are no longer able to do so.

<sup>34</sup> In 2015, a childless taxpayer can receive a maximum credit of \$503, while the maximum values of the credit for taxpayers with children are \$3,359 for a taxpayer with one child, \$5,548 for a taxpayer with two children, and \$6,242 for a taxpayer with three or more children. These levels are adjusted annually for inflation. For more information, see CRS Report R43805, *The Earned Income Tax Credit (EITC): An Overview*, by Gene Falk and Margot L. Crandall-Hollick. It is possible that low-income couples with children could have a marriage tax bonus if they were in the phase-in range for the EITC.

<sup>35</sup> Currently, the phase-out threshold is \$110,000 for couples filing jointly and \$75,000 for unmarried individuals.

<sup>36</sup> For general background on the adoption tax credit, see CRS Report RL33633, *Tax Benefits for Families: Adoption*, by Noah P. Meyerson.

### ***Non-Taxable Employee Compensation***

Federal recognition of same-sex marriage also affects whether certain forms of employee compensation of individuals in a same-sex marriage are nontaxable, including contributions to dependent care flexible spending accounts (DCFSA) and the employer contributions for employer-provided health insurance plans.

Under current law, taxpayers with children may contribute up to \$5,000 to a DCFSA. The total amount of contributions that are tax exempt for any tax return is \$5,000 without regard to the number of children or the number of parents. Hence, a married couple can put a maximum of \$5,000 in a DCFSA, the same maximum amount an individual can put in these accounts. Therefore, any amount in excess of \$5,000 would be included in taxable income for the married couple.<sup>37</sup>

In contrast to the effect on DCFSA, married same-sex couples who are covered by an employer-sponsored health insurance plan may receive tax benefits. When an employee elects to purchase employer-provided health insurance, the employer generally pays for part of the premium. The employer's contribution to an individual or family plan generally is not considered taxable income to the employee. Before federal recognition of same-sex marriages, same-sex employees who purchased an employer-sponsored family health plan were taxed on the estimated value of the employer's contribution toward the premiums for the same-sex spouse; however, opposite-sex married couples were not taxed on the portion of health insurance premiums the employer paid for the opposite-sex spouse. Now, the estimated value of the employer's contribution to health-insurance coverage for an employee's same-sex spouse is nontaxable, thus reducing tax liability.

### **Potential Federal Tax Revenue Consequences of Federal Recognition of Same-Sex Marriage**

Federal recognition of same-sex marriages affects federal tax revenues primarily through changes in the federal income tax. For the limited number of married same-sex individuals who have sufficient assets to be subject to the estate tax, potential estate tax liability may also be affected. While it did not change the administration of federal income tax laws, the *Obergefell* decision may affect *the number* of same-sex couples who decide to marry (and hence the number of couples who file their federal and state tax returns as married).

Research quantifying the income tax consequences of marriage for opposite-sex couples may be useful for understanding the potential tax revenue consequences of federal recognition of same-sex marriage. Applying the 2007 tax code to cohabiting couples, Lin and Tong (2012) found that roughly half of couples who marry would have a marriage tax penalty.<sup>38</sup> Most of the remaining couples (38%) were estimated to have marriage tax bonuses. On average, marriage resulted in an increase in tax liability of \$450 per couple. Other research, using 2009 data, found that more than

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<sup>37</sup> For tax returns filed immediately after *Windsor*, same-sex married couples who each had contributed to a DCFSA may have found that part of their account became taxable even though their individual incomes made them eligible for the child and dependent care credit. If each partner had a child and each was contributing to a DCFSA, they may have over-contributed in the first year in which they filed as a married couple. In subsequent years, married same-sex couples (like married opposite sex couples) are limited to putting \$5,000 in the DCFSA, though they could divide that amount between themselves. Filing separate returns would be the least beneficial because no child care expenses are recognized for married people who file separately.

<sup>38</sup> Emily Y. Lin and Patricia K. Tong, "Marriage and Taxes: What Can We Learn from Tax Returns Filed by Cohabiting Couples?" *National Tax Journal*, vol. 65, no. 4 (December 2012), pp. 807-826.

half of couples had a marriage bonus (54%), with 38% of couples having a marriage tax.<sup>39</sup> In this study, the average couple experienced a marriage subsidy of \$671 in 2009. Alm and Leguizamon (2015) also found that the proportion of couples likely to face a marriage tax penalty or bonus has changed over time, with more couples receiving a bonus in the late 2000s as compared to the late 1990s or early 2000s. Other research notes that because the demographic characteristics of opposite-sex couples differ from those of same-sex couples (e.g., within-couple distribution of earnings, number of children), marriage tax consequences among the population of same-sex couples may not follow the same patterns as found for opposite-sex couples.<sup>40</sup>

As discussed earlier in this report, if same-sex couples tend to have two income earners with similar incomes, these couples are more likely to face marriage tax penalties, especially if their combined income were to push them above the 15% tax bracket. On the other hand, same-sex couples who marry are less likely to have children prior to marriage than opposite-sex couples who marry, which would lead to fewer same-sex couples receiving marriage tax penalties in comparison to opposite sex couples.<sup>41,42</sup>

On balance, as indicated by the estimates that suggest federal recognition of same-sex marriage will result in additional federal revenues,<sup>43</sup> the value of marriage tax penalties is expected to exceed the total value of marriage tax bonuses for same-sex couples.<sup>44</sup> Reportedly, Treasury has noted that data on the proportion of married same-sex couples who would face marriage tax penalties or bonuses is lacking.<sup>45</sup>

For federal income tax purposes, federal recognition of same-sex marriage will likely result in additional federal income tax revenues, although available estimates suggest the budgetary impact would be small. Before the *Windsor* decision, there were several estimates of the changes in revenues that would result from recognizing married same-sex couples as married for federal tax purposes. In 2004, the Congressional Budget Office (CBO) estimated that recognition of same-sex marriages would increase federal income tax revenues by \$200 million to \$400 million per year between 2005 and 2010.<sup>46</sup> Others maintained that the revenue gains would be smaller than

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<sup>39</sup> James Alm and J. Sebastian Leguizamon, “Wither the Marriage Tax?,” *National Tax Journal*, vol. 68, no. 2 (2015), pp. 251-280.

<sup>40</sup> Differences in demographic characteristics between same-sex and opposite-sex couples are noted in Adam Stevenson, “The Labor Supply and Tax Revenue Consequences of Federal Same-Sex Marriage Legalization,” *National Tax Journal*, vol. 65, no. 4 (December 2012), pp. 783-806.

<sup>41</sup> Stevenson, *supra* note 40.

<sup>42</sup> Generally, when a couple has children before marriage, one parent files as head of household claiming the children and the other files as single. Such couples may find that once married they will be in a higher tax bracket since tax brackets above the 15% bracket for married couples filing jointly are less than the combined levels if one of the taxpayers were filing as head of household and the other as single (see **Table 2**). Hence marriage among a couple that already has children before marriage is more likely to lead to a marriage penalty in comparison to a similarly situated couple without children. In addition, among low-income couples with children prior to marriage, marriage can result in those couples receiving a smaller EITC, and hence also result in a marriage penalty.

<sup>43</sup> Congressional Budget Office, *The Potential Budgetary Impact of Recognizing Same-Sex Marriages*, Washington, DC, June 21, 2004, <http://www.cbo.gov/publication/15740> and Stevenson, *supra* note 40.

<sup>44</sup> Over time, the social and economic characteristics of same-sex couples who legally marry may change. For example, more married same-sex couples may choose to have or adopt children. Or one spouse may choose to leave the workforce. Such changes could have an impact on the federal income tax liability of the couple.

<sup>45</sup> Beyoud, *supra* note 15.

<sup>46</sup> Congressional Budget Office, *The Potential Budgetary Impact of Recognizing Same-Sex Marriages*, Washington, DC, June 21, 2004, <http://www.cbo.gov/publication/15740>.

CBO's estimates, somewhere in the \$20 million to \$40 million range annually.<sup>47</sup> A more recent study estimated an annual reduction in federal revenues of between \$187 million and \$580 million, depending on whether the taxpayers minimized their tax liabilities (by for example, itemizing their deductions) or took the standard deduction.<sup>48</sup> Relative to the magnitude of total individual income tax revenues—\$1.4 trillion in 2014—the federal revenues raised by recognizing same-sex marriages represent less than one-tenth of one percent of income tax revenues.<sup>49</sup>

## Amending Tax Returns After *Windsor*

Before the 2013 IRS ruling, all same-sex married couples were required to file their federal income tax returns as unmarried individuals. However, the IRS made clear that taxpayers who were in same-sex marriages for one or more open prior tax years could file amended returns to change their filing status to that of a married couple. At the time of the 2013 IRS ruling, this meant that amended returns could be filed for tax years 2010, 2011, and 2012.<sup>50</sup> As of the date of this report, tax year 2012 is still an open year, and tax year 2011 may still be an open year if the original 2011 return was filed on extension.

Filing amended returns for tax years before 2013 to reflect their marital status is an option, but not a requirement of married same-sex couples. Thus, in these cases taxpayers may choose to file an amended return if doing so will result in a refund.<sup>51</sup>

Taxpayers in same-sex marriages who want to amend prior year's tax returns for reasons other than changing their filing status may proceed with caution since it is unclear whether they are required to change their filing status if amending the return after September 16, 2013.<sup>52</sup> If such a change in filing status were required, it might negate any benefit they would otherwise derive from amending the return depending upon the facts and circumstances involved in their (and their spouses') returns. Surviving spouses of same-sex marriages may choose to file an amended estate tax return for open years if the decedent's estate was subject to estate taxes as a result of not using the unlimited marital deduction.

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<sup>47</sup> Stevenson, *supra* note 40.

<sup>48</sup> James Alm, J. Sebastian Leguizamon, and Susane Leguizamon, "Revisiting the Income Tax Effects of Legalizing Same-Sex Marriages," *Journal of Policy Analysis and Management*, vol. 33, no. 2 (Spring 2014), pp. 263-289.

<sup>49</sup> Others have also noted that while recognizing same-sex marriages for federal tax purposes will likely result in additional federal revenues, the effect is expected to be small. See Diana Furchtgott-Roth, "Same-Sex Marriage Decisions Won't Affect Uncle Sam's Bottom Line," *Tax Notes*, July 1, 2013, pp. 75-77. For federal revenues from the individual income tax, see the Tax Policy Center, TPC Tax Facts, Historical Amount of Revenue by Source, available at <http://www.taxpolicycenter.org/taxfacts/displayafact.cfm?Docid=203>.

<sup>50</sup> Generally, taxpayers may file amended returns within the three years after the filing date of the return or two years after the tax was paid, whichever is later. These are considered "open years." Note that there may be other considerations in determining whether to amend a prior year's return beyond obtaining a refund.

<sup>51</sup> Taxpayers may also choose to file amended returns to exclude from income certain fringe benefits, such as health insurance coverage, provided to a same-sex spouse. Where health insurance for a same-sex spouse was included in income, the taxpayer may be able to recover excess Social Security and Medicare taxes paid based on the income recognized for the same-sex insurance coverage. Employers will be able to file Form 941-X to claim refunds or adjustments for overpayment of both the employer's and employee's portions of Social Security and Medicare tax. The IRS is expected to provide guidance soon regarding procedures to be followed. *Answers to Frequently Asked Questions for Individuals of the Same Sex Who Are Married Under State Law*, Q. 12, Internal Revenue Service. Available at <http://www.irs.gov/uac/Answers-to-Frequently-Asked-Questions-for-Same-Sex-Married-Couples>.

<sup>52</sup> IRS guidance addresses the effect of *Windsor* on original returns filed after September 15, 2013, as well as the option for amending to change the filing status on a return to MFJ or MFS, but does not address whether an amended return filed after September 15, 2013 *must* be filed using a married filing status. *Id.* Q. 2.

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## Acknowledgments

Former CRS legislative attorney Carol A. Pettit authored a portion of this report.

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